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RUEHMO/AMEMBASSY MOSCOW 6151
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RUEHLU/AMEMBASSY LUANDA 0974
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RUEHWR/AMEMBASSY WARSAW 0854
RUEHBR/AMEMBASSY BRASILIA 2054
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RUEHAK/AMEMBASSY ANKARA 0951
RUEHTV/AMEMBASSY TEL AVIV 0001
RUEHSA/AMEMBASSY PRETORIA 1569
RUEHCU/AMEMBASSY KUWAIT 0235
RUEHAD/AMEMBASSY ABU DHABI 0263
RUEHPL/AMEMBASSY PORT LOUIS 0974
RUEHPS/AMEMBASSY PRISTINA

UNCLAS SECTION 01 OF 11 PARIS 001423

SENSITIVE
SIPDIS

STATE FOR EEB/IFD/OMA
TREASURY FOR DO/IDD AND OUSED/IMF
SECDEF FOR USDP/DSCA
PASS EXIM FOR CLAIMS - MPAREDES
PASS USDA FOR CCC -- ALEUNG/WWILLER/JDOSTER PASS USAID FOR CLAIMS --
WFULLER
PASS DOD FOR DSCS -- PBERG

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SUBJECT: PARIS CLUB - JULY 2008 TOUR D'HORIZON AND DISCUSSIONS ON
METHODOLOGICAL ISSUES

1. (SBU) Summary: At the Paris Club's July 7-8 session, the Vice Chairman briefed creditors on his recent meetings in Kinshasa with the Ministers of Economy and Finance, noting concern that a proposed infrastructure deal involving a DRC sovereign guarantee was at odds with the Paris Club's projected cancellation of \$5 billion in debt at completion point. The Secretariat reported continuing discussions with the IMF over how to handle Grenada's poor 2007

performance on its Poverty Reduction and Growth Facility (PRGF) and whether the second phase of the country's May 2006 rescheduling in the Paris Club should enter into force. On Iraq, neither the IMF nor Bank had specifics on the reported UAE/Iraq debt agreement. The Secretariat noted the final phase of Iraq's 2004 Paris Club agreement will enter into force in December if the country continues to perform satisfactorily on its current IMF Stand-By Arrangement (SBA).

¶2. (SBU) During the Tour d'Horizon, the U.S. and other creditors also discussed relations with Burundi, Congo-B, Guinea, Kosovo, Libya, the Seychelles, and Togo. Several members submitted issues for Paris Club consideration, including illegitimate debt and a submission to the Doha Financing for Development conference. The Club's long-standing policy on leasing was revisited at the request of the Italians; however, with lack of consensus on the issue, the Secretariat agreed to send out questionnaires to creditors and prepare a working paper for further discussion in September. End Summary.

¶3. (U) For additional information on a specific country or issue, please contact Nicholle Manz or David Freudenwald in EEB/IFD/OMA.

Burundi

PARIS 00001423 002 OF 011

¶4. (SBU) The IMF reported that a new PRGF program had been approved on July 7, which paved the way for the Paris Club to resume interim HIPC relief. Creditors will need to decide in September whether to retroactively extend the consolidation period of the previous Paris Club agreement, or negotiate a new agreement with Burundi that would fold in arrears. For now the IMF is assuming that the Paris Club will apply existing terms by retroactively extending the previous consolidation period. Should Burundi require a new agreement, negotiations would likely take place in October. The IMF said Burundi could reach its HIPC completion point in late 2008 or early ¶2009.

Congo-Brazzaville

¶5. (SBU) The Secretariat reported that Congo-B authorities have not responded to the Paris Club Co-Chairman's April 2008 letter asking about press reports of an agreement with litigating creditors. The IMF said a new PRGF program could come to the Executive Board as early as mid-October if Congo performs well on its January-June 2008 Staff-Monitored Program. PRGF discussions began in May 2008 and an August IMF mission will assess performance. IMF and Bank Boards will discuss HIPC triggers in September. The Bank noted work on debt management, including data centralization and a debt management capacity mission. A new Country Assistance Strategy should be ready in 2009. A new PRGF program would trigger the resumption of interim HIPC relief. As in the case of Burundi, creditors will have to decide whether to retroactively extend the consolidation period of the previous Paris Club agreement or negotiate a new agreement. The Secretariat asked creditors whether they had received any payments from Congo during the off-track period and several, including the U.S., reported receiving a portion of amounts due.

PARIS 00001423 003 OF 011

DRC

¶6. (SBU) The Paris Club's Vice Chairman briefed creditors on his recent Ministerial meetings in Kinshasa. DRC authorities acknowledged that a new, large investment deal involves a sovereign guarantee, but they argued that the financing is sufficiently concessional to not significantly effect the Paris Club rescheduling

agreement. An IMF team, however, is assessing this issue because the size of the project could impact debt sustainability. The Paris Club is set to cancel approximately \$5 billion in debt at completion point. The authorities appear to understand the need for greater transparency and are sharing information with the IMF and World Bank in an attempt to finalize the deal without jeopardizing their aspiration of reaching HIPC completion point.

Grenada

17. (SBU) The Secretariat reported ongoing discussions with the IMF on Grenada. At issue is whether the Paris Club should enter into force the second phase of Grenada's May 2006 rescheduling, which covers maturities falling due in 2007. Given Grenada's poor performance on its PRGF in 2007, the Paris Club is contemplating not allowing the second phase to enter into force. The IMF expressed concern last month that such a decision would be tantamount to withdrawing financing assurances and could jeopardize the financing of future IMF programs for countries in similar situations. The Secretariat acknowledged that the Paris Club's decision on Grenada would have implications for Paris Club policy going forward. Canada asked whether creditors could assume that the third phase of Grenada's agreement, covering 2008 maturities, would enter into

PARIS 00001423 004 OF 011

force. The Secretariat said yes, but planned to inform the authorities after the Club's decision about the second phase.

Guinea

18. (SBU) The Secretariat reported that, ahead of the July 31 deadline, Guinea has concluded, or is on the verge of concluding, with its Paris Club creditors bilateral agreements implementing the January 2008 Agreed Minute on Cologne terms. (The US bilateral agreement entered into force in June.) Brazil's agreement could be completed in the next two months; Russia's would be done "pretty soon"; Spain will sign within a few weeks; and Germany is awaiting the GOG's response to a draft agreement. In addition, Guinea has contacted all of its non-Paris Club creditors and thus far has concluded bilateral agreements with Romania and Libya, while making progress with China, the Saudi Fund for Development, and the Kuwait Fund (these three plan to conclude an agreement after Guinea reaches completion point). The Secretariat proposed sending letters to Bulgaria, Egypt, Morocco, and Thailand encouraging comparable treatment. The IMF said Guinea has largely met its PRGF program targets, despite external shocks and domestic political instability. The Board will hold the first PRGF program review for Guinea on July 28; discussion of HIPC triggers and the second review will take place in the fall; and Guinea could reach its HIPC completion point by the end of the year.

Haiti

19. (SBU) Creditors supported the Secretariat's draft response to an open letter from NGOs to European heads of state and government

PARIS 00001423 005 OF 011

calling for immediate debt cancellation for Haiti. Several creditors suggested minor changes to the content and tone of the response. The Secretariat will send a revised version that, taking into account non-European Paris Club members, addresses Paris Club members' generous support for Haiti without referring to European recipients of the letter.

Iraq

¶10. (SBU) The Secretariat clarified that if Iraq continues to perform satisfactorily on its SBA, the third and final phase of its 2004 Paris Club agreement will enter into force in December, raising the level of cancellation from 60% to 80%. The IMF noted that the SBA was tailored to satisfy the Paris Club's requirement of three consecutive years of performance: the mid-June mission reached broad ad-ref agreement on required steps; the first review will be on September 5; the second in November/December, and the third by the end of the year. Neither the IMF nor Bank had specifics about reports of an UAE/Iraq debt agreement. (Brazil attended the discussion but was not asked about its failure to provide comparable treatment.)

Kosovo

¶11. (SBU) The World Bank reported that the Kosovo Debt Management Support Program (KDMSP) was approved on July 3, in a contentious Board decision. The World Bank noted that the US was prepared to contribute \$125 million to the IDA-administered trust fund set up to finance the KDMSP. Debt related to Bank projects on Kosovar soil amounts to approximately \$615 million currently, i.e., nearly half

PARIS 00001423 006 OF 011

of an estimated \$1.3 billion in external debt that Serbia notionally attributes to Kosovo. To date, Serbia has been servicing Kosovo's debt. The IMF has been providing technical assistance to Kosovo under a 1999 Board decision. Once the IMF completes its poll to confirm a majority of its membership recognizes Kosovo as an independent country, the IMF planned to accept Kosovo's application for membership (Kosovo later submitted its application to the Fund and Bank on July 10.) Russia stated that Kosovo is not a sovereign state, so there should not be discussion of separate issues or documents regarding Kosovo. The US said it recognized Kosovo's independence in February 2008, asked the Secretariat about sharing loan documentation with the authorities in Pristina, and welcomed the World Bank's decision to establish trust funds for budget support and debt relief. Given that the Serbian government has changed since the Secretariat sent its May 2007 letter about sharing loan information, the Secretariat offered to send a new letter regarding this issue.

Liberia

¶12. (SBU) The IMF said Liberia met with its commercial creditors in April and was likely to pursue a buyback operation through IDA's Debt Reduction Facility (DRF). The IMF noted that Liberia had also contacted its non-Paris Club bilateral creditors. The World Bank said it was prepared to finance a large portion of a DRF operation and was eager to move forward as soon as possible. The Bank is providing \$1.3 million to fund the debt advisory group, which is negotiating with Liberia's commercial creditors; the Bank will seek the advisors' views on the timetable. A DRF operation would involve about \$48 million, or 3% of the \$1.6 billion in commercial debt outstanding. Of the \$48 million, Liberia is asking donors to provide \$25 million. President Johnson-Sirleaf wrote to seven

PARIS 00001423 007 OF 011

countries asking for contributions: Germany, Japan, Norway, Sweden, Switzerland, UK, and the US. Norway will respond positively to a Liberian request for a \$5 million contribution.

Libya

¶13. (SBU) In June, the Secretariat promised to contact the authorities to find out whether the finance minister intends to respond to the Paris Club's January 2008 letter, which expressed concern that Libya had concluded bilateral agreements with certain creditors while remaining in default toward seven Paris Club

creditors. Libya asked to postpone a scheduled July 7 meeting with the Secretariat.

Seychelles

¶14. (SBU) The IMF confirmed that the Seychellois finance minister has written a letter to request an IMF program. The authorities were motivated by a desire to address the country's public debt. The IMF said the authorities have been taking steps in the right direction, including exchange rate depreciation vis-a-vis the dollar. The Bank is providing technical advisory services in key areas. A mission in the field is discussing an interim strategy to support an IMF program which, in turn, would open the door to a Paris Club debt treatment under the Evian approach.

Togo

PARIS 00001423 008 OF 011

¶15. (SBU) Following Togo's Naples treatment in June, and considering that Togo could reach HIPC decision point as early as this fall, creditors debated whether to conclude two separate bilateral agreements (per usual practice) or wait until decision point and conclude a single bilateral agreement. While last month's Naples agreement established a deadline for concluding bilateral agreements, creditors could choose to wait until decision point to conclude a single agreement. Since June, the Bank has provided \$17 million for rural community development and food security and \$3 million to offset food price increases; in September, the Board will discuss additional steps to address the food crisis.

Methodological Discussions:
Paris Club's Policy on Leasing

¶16. (SBU) At Italy's request, the Paris Club discussed its long-standing policy on leases. The Secretariat described the key considerations that led creditors to decide two decades ago to exclude leases from Paris Club treatments and noted that lease activity has since increased significantly. In order to make an accurate assessment of risk, Italy said it was important to have a clear picture of how leases could be treated in the Paris Club and believed the risk assessment should not be affected by the type of financing chosen. Some creditors expressed willingness to review the policy. The UK added its ECA's view that the current policy was fine. The U.S. stated that the current policy was working well and should not be changed. The Secretariat noted the merit of conducting the exercise, despite the lack of consensus, and said it would proceed with a questionnaire and preparation of a Working Paper for discussion in September.

PARIS 00001423 009 OF 011

Methodological Discussions: Proposed Work Program

¶17. (SBU) At the invitation of the Secretariat, creditors proposed a number of methodological issues that the Paris Club could tackle in coming months.

-- Italy suggested submitting a written statement to the Doha conference on Financing for Development in November 2008 to highlight the Paris Club's contributions related to the "External Debt" pillar (e.g., HIPC initiative, debt sustainability, Evian approach, litigating creditors, and outreach to emerging creditors). Italy suggested that the Paris Club meet with the OECD's Export Credit Group and its Development Assistance Committee (DAC) in September/October to discuss lending guidelines and soft loans,

which could be channeled into the Financing for Development process.

-- Germany called for a closer look at the concept of illegitimate debt, noting Ecuador's debt commission and NGO, UN and other discussions on this issue. Norway supported this idea, but the UK warned that, given that it is a highly contentious, politically-charged concept, there should be an ample exchange of views before the Secretariat contemplates drafting a Working Paper.

-- Spain suggested a study of Paris Club versus non-Paris Club lending and examination of how to deal with countries that do not want IMF programs, citing Angola, Argentina, and Cuba.

-- The Netherlands proposed further discussion of approaches to debtor countries, noting lack of proper instruments for dealing with countries facing debt repayment profile problems.

-- Japan agreed generally with the proposals and suggested examining

PARIS 00001423 010 OF 011

prepayments and buybacks, the Paris Club's relations with non-Paris Club creditors, and fragile states.

-- The US asked about the status of the two possible working groups that Chairman Musca proposed during the June meeting with the private sector. The Secretariat is planning an informal meeting in October with the eight non-Paris Club creditors invited to the June private sector meeting and other non-Paris Club official creditors in order to solicit views on Paris Club policies. If this first step succeeds, the Secretariat plans to organize a more formal plenary. As for formation of a group with private creditors to discuss vulture funds, the Secretariat has contacted the Institute for International Finance to discuss a possible work agenda. The US also asked to revisit comparability of treatment related to buybacks.

¶18. (SBU) The Secretariat stated it could not tackle all of these issues, noting concern about whether the Paris Club was the correct forum to address some of them. It expressed doubt about addressing the difficult topic of illegitimate debt (and agreed even a Working Paper would be premature) or discussing accounting rules and soft loan guidelines with the DAC. The Secretariat will compile a list of all the suggestions submitted, establish an order of priority, and identify possible deliverables, including in particular the Doha FfD submission.

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Attendance of Representatives From Multilateral
Institutions at Paris Club Negotiations
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¶19. (SBU) Creditors debated whether to allow representatives from institutions other than the IMF and World Bank to be present for the duration of Paris Club negotiations with debtor countries.

PARIS 00001423 011 OF 011

Currently, observers from organizations other than the IMF and World Bank leave the negotiation, along with the debtor country, when the internal discussions among creditors begin. The Secretariat concluded that current practice would continue.

STAPLETON